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Environmental Review at Export Development Canada

October 2004



Office of the Auditor General of Canada
Bureau du vérificateur général du Canada



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Office of the Auditor General of Canada
240 Sparks Street, Stop 10-1
Ottawa, Ontario
K1A 0G6

Telephone: (613) 952-0213, ext. 5000, or 1-888-761-5953

Fax: (613) 954-0696

E-mail: distribution@oag-bvg.gc.ca

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Auditor General of Canada
Vérificatrice générale du Canada

To the Honourable Speaker of the House of Commons
To the Honourable Speaker of the Senate

I have the honour to transmit herewith my Report on the audit under subsection 21(2) of the *Export Development Act* of the Environmental Review Directive and other environmental review processes established by Export Development Canada. I have submitted this report to the Minister of International Trade and to the Board of Directors of Export Development Canada.

A handwritten signature in cursive script that reads "Sheila Fraser".

Sheila Fraser, FCA

Ottawa, 26 October 2004



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Environmental Review at Export Development Canada

Main Points

1. We found that the Environmental Review Directive and other environmental review processes used by Export Development Canada include most elements of a suitably designed environmental review procedure. We identified these key design elements based on a review of the documented policies of similar institutions. EDC's current review policies meet more standard design elements than its previous policy.
2. We found major improvements in the manner in which EDC implemented its environmental review processes, including the Directive, over a similar audit conducted in 2001. Overall, we concluded that the Directive and EDC's other environmental review processes were operating as designed.
3. EDC designed the Directive to allow it to exercise discretion in the many steps involved in its implementation. We were satisfied that EDC was careful in exercising its professional judgment in categorizing transactions and in making its determinations under the Directive. At the same time, we noted areas for improvement in documenting how it exercises this discretion in its review of environmental impact assessment reports and public consultation.
4. Increased expectations for greater accountability in both the private and public sectors impose on EDC a greater responsibility to demonstrate that it exercises its discretion wisely. In our view, the counterbalance to the broad discretion in EDC's environmental review policies is greater transparency. Although EDC filled some of the transparency gaps we noted previously, our Report recommends additional steps that EDC needs to take to enhance transparency and to assure Parliament and Canadians that EDC's environmental review processes uphold high standards of environmental protection and sustainable development.
5. In our 2001 Report, we found that EDC was a leader among its counterparts. Now, EDC has designed its environmental review policies to be in line with the *Recommendation on Common Approaches on Environment and Officially Supported Export Credits* of the Organisation for Economic Co-operation and Development (OECD). While EDC is ahead of its counterparts in requiring third party review of environmental impact assessment reports, other export credit agencies show leadership by exceeding the OECD Common Approaches for disclosure and public consultation elements. These are the two areas we highlighted in our last Report and that EDC still needs to improve. In our view, EDC should decide whether it wishes

to show leadership among export credit agencies by enhancing its Directive and other review processes.

Background

6. Amendments in 2001 to the *Export Development Act* imposed a legal obligation on EDC to carry out environmental reviews of project-related transactions. EDC adopted a new Environmental Review Directive in 2001 and established supplementary environmental review processes for certain transactions not covered by the Directive. Our audit examined the design and implementation of these environmental review processes.

7. This is our second Report on EDC's environmental review processes. Our first Report in May 2001 found that EDC's Environmental Review Framework had most elements of a suitably designed environmental review process, although there were important gaps in public consultation and disclosure. We also found significant differences between the Framework's design and its operation and concluded that the Framework was not operating effectively.

8. EDC and other export credit agencies do business in a climate of escalating expectations regarding transparency, public trust, and accountability. Their role in international finance, particularly in the developing world, has brought increased pressure from stakeholders to develop more stringent standards for carrying out environmental and social reviews of projects that they finance. In 2003, members of the OECD adopted the Organisation's *Recommendation on Common Approaches on Environment and Officially Supported Export Credits*. This document promotes a level playing field for officially supported export credits by establishing common procedures and processes for environmental reviews of projects while respecting the primary role of export credit agencies to promote trade in a competitive environment.

Export Development Canada has responded. Export Development Canada has accepted, and agreed to take action on, all our recommendations. It has provided a response for each recommendation as well as an overall comment. Each response includes a statement of actions either taken or planned.

Introduction

Overview of Export Development Canada

9. Export Development Canada (EDC) is a Crown corporation whose mandate is to support and develop Canada's export trade and Canadian capacity to engage in that trade, and to respond to international business opportunities. EDC operates as a commercial financial institution to provide trade finance and risk-mitigation services to Canadian exporters and investors (Exhibit 1).

Did you know?

EDC's 2003 business activity

Amount of exports and international investments supported by EDC: **\$51.9 billion**

Percentage of Canada's gross domestic product that EDC's business volume represents: **3.4%**

Number of countries where it supported sales and investments: **over 170**

Number of which were developing countries: **143**

Percentage of business volume that is in developing countries: **20%**

Percentage of business volume that is in small- and medium-sized business: **20%**

Percentage of customer base that is small- and medium-sized business: **91%**

Exhibit 1 Export Development Canada's business activities

Export Development Canada offers a range of financial and credit insurance services to Canadian exporters and investors, including

- short-term insurance, such as accounts receivable insurance that protects against the risk of non-payment (over 70 percent of EDC's business is in short-term accounts receivable transactions);
- contract insurance and bonding to guarantee bids for goods and services;
- direct loans to foreign buyers; and
- political risk insurance against transfer of funds, expropriation, and political violence.

EDC also administers the Canada Account for the federal government. The Canada Account supports export trade transactions that involve risks, and amounts or terms that fall outside EDC's lending or insurance criteria. It represents a small portion of EDC's business volume. Transactions must be authorized by the Minister of International Trade and agreed to by the Minister of Finance. EDC's Board of Directors ensures that these transactions are administered appropriately.

Source: Export Development Canada

10. EDC has developed tools, practices, and policies to manage risk in the export transactions it considers. EDC has also adopted environmental review processes to meet its legal obligation under its legislation, to manage environmental risk, and to ensure that the transactions it supports are justified after consideration of environmental issues.

Our 2001 Report

11. In May 2001, we released our Report on the design and implementation of the environmental review policy and procedures EDC used at the time. This policy was known as the Environmental Review Framework.

12. We reported that while the Framework had most elements of a suitably designed environmental review process, there were important gaps in public consultation and disclosure. We also found significant differences between the Framework's design and its operation and concluded that the Framework was not operating effectively. The Report contained recommendations for improvements to both the design and implementation of the Framework. EDC undertook to address these recommendations.

Civil society groups—Non-profit associations that operate independent of the government. They can include universities, environmental movements, indigenous peoples' groups, communities and trade unions.

Changes since May 2001

13. Consultation. In response to our Report, EDC consulted with business and **civil society groups** from across Canada in 2001 on revisions to its environmental review process. EDC used three documents for these initial consultations: a draft document from the Organisation for Economic Co-operation and Development (OECD), a guidance document prepared by the Department of Foreign Affairs and International Trade, and a consultant's paper focussing on broad issues relating to environmental review.

14. New legal obligation. In the meantime, Parliament amended the *Export Development Act*. The amendments, which came into effect on 21 December 2001, established a legal requirement for EDC's board of directors to issue a directive to assess the environmental effects of project transactions. EDC released its new Environmental Review Directive the same day.

15. Additional consultation. In 2002, EDC gave the public an opportunity to comment on the Directive and a draft policy on prior disclosure of environmental and social impact information. After a 60-day consultation period, EDC made minor changes to the Directive, but substantially altered its draft prior disclosure policy. It dropped the proposed 45-day period for disclosing information and the condition making consent for disclosure from Canadian project sponsors a requirement for EDC support. EDC made these changes in response to concerns from the business community that EDC maintain a level playing field with other export credit agencies. The amended Directive and new prior disclosure policy both came into effect on 1 May 2002.

16. Other changes. EDC made other operational changes in response, among other things, to our Report. It created supplementary processes to review the environmental impacts of certain transactions not subject to the Directive. It hired a Chief Environmental Advisor to direct a team of in-house environmental specialists to review transactions under the new Directive and its other environmental review processes. And in 2002, EDC established a new position of Compliance Officer. This officer responds directly to public inquiries and oversees issues and policies on transparency and disclosure practices, human rights, business ethics, and the environment.

Evolving international and domestic context

17. External pressure. Export credit agencies such as EDC play a key role in international trade and finance in developing countries. Collectively, they represent a large source of public international finance and provide an important tool for large-scale infrastructure and resource extraction projects in the developing world.

18. This prominent role has brought increased scrutiny from civil society groups concerned about the potential significant environmental and social impacts of these investments. These groups have demanded that export credit agencies develop more stringent standards for carrying out environmental and social reviews of projects and that they make their reviews

more transparent. Two initiatives in particular show the response of export credit agencies and the private banking sector to the call for enhanced standards and greater transparency in their application.

19. Organisation for Economic Co-operation and Development. The Working Party on Export Credits and Credit Guarantees has operated under the auspices of the OECD to create coherence among the environmental risk assessment practices of export credit agencies. In December 2003, Canada and other OECD member countries adopted the *OECD Recommendation on Common Approaches on Environment and Officially Supported Export Credits*. This document promotes a level playing field for officially supported export credits by establishing common procedures and processes for environmental reviews of projects. The OECD Common Approaches aims to promote good environmental practices with a view to achieving a high level of environmental protection. It recommends that members seek to foster transparency, predictability, and responsibility in decision-making by encouraging disclosure of relevant environmental information while taking into consideration business confidentiality and other competitive concerns. Although OECD recommendations are not legally binding, there is an expectation that OECD member countries will act in good faith to fully implement them.

20. Equator Principles. In 2003, the private banking sector developed the Equator Principles, a set of voluntary guidelines to help the banking industry address environmental and social risks in large-scale project financing. Based on policies and guidelines of the World Bank and the International Finance Corporation, the Principles apply to projects with a total capital cost of US\$50 million or more in all industry sectors throughout the world.

21. As at 15 April 2004, 21 banks (including 2 Canadian banks) had adopted the Principles. Banks, like export credit agencies, are a source of project finance. Market analysts calculate that the banks adopting the Principles represented approximately 75 percent of the project loan market volume in 2003. In May 2004, Denmark's Eksport Kredit Fonden became the first export credit agency to adopt the Principles.

22. EDC's actions in adopting the Directive and in making the changes noted above are consistent with the trend toward enhanced accountability and transparency of financial institutions in Canada and abroad. Exhibit 2 shows some of the developments over the past few years in Canada and internationally that have influenced changes in the environmental review policies of export credit agencies.

EDC's Environmental Review Directive and other environmental review processes

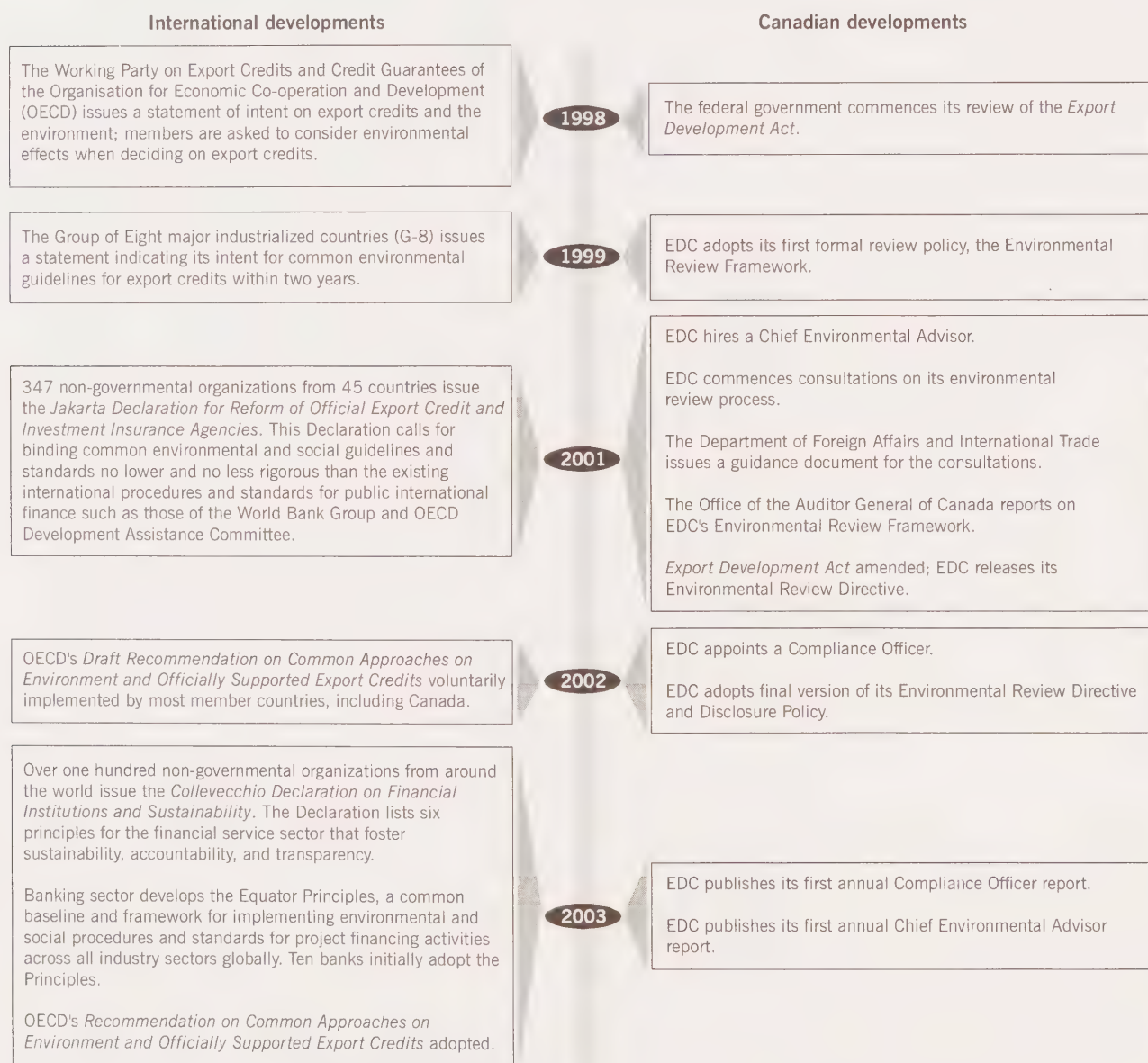
23. Key elements. EDC's environmental risk management process has two components:

- the Environmental Review Directive to respond to EDC's legal obligation to carry out environmental reviews of transactions in accordance with the *Export Development Act*, and

- supplemental processes to conduct environmental reviews of transactions that do not fall within the scope of the Directive.

24. The Directive. The Directive establishes the scope of EDC's legal obligation to carry out environmental reviews of project-related transactions. It requires EDC to categorize projects on the basis of their potential adverse environmental effects. It also requires EDC to determine whether a project is likely to have adverse environmental effects despite mitigation measures and then whether EDC is nonetheless justified in entering into the transaction.

Exhibit 2 Canadian and international developments in the environmental review policies of export credit agencies—A timeline



No such determination is required for lower risk projects. Nor is one required for projects in Canada or the United States, provided EDC receives confirmation that such projects are designed to meet host country environmental requirements.

25. The Directive is publicly available on EDC's Web site at www.edc.ca and a copy is set out in the Appendix. Exhibit 3 sets out the steps EDC follows in applying its Directive.

Exhibit 3 Elements of EDC's Environmental Review Directive

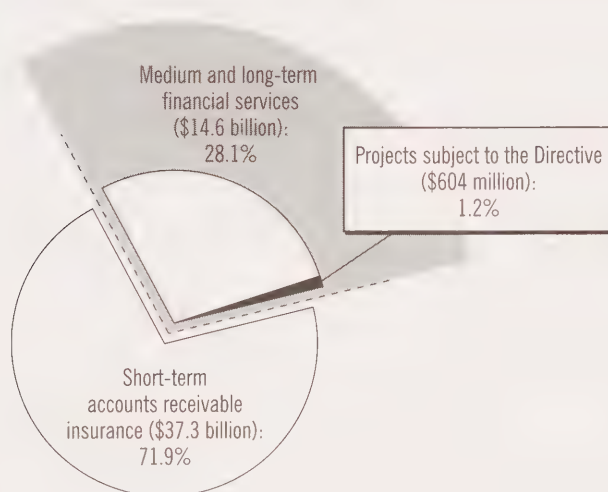
Screening	The Directive applies to financing, political risk insurance, or equity transactions. Transactions must be related to a project, have a value of over SDR10 million*, and have a repayment term of over two years. A project is "a physical development that is greenfield [undeveloped], or undergoing major extension or conversion and is industrial, commercial, or infrastructure-related in nature."
Categorization	<p>Projects are categorized according to their potential adverse impacts:</p> <p>Category A. The project is likely to have significant adverse environmental effects that are sensitive, diverse, or unprecedented. Effects may affect a broader area than the project site and be irreversible. (Annex 1 of the Directive lists examples of these projects.)</p> <p>Category B. The project is likely to have less adverse environmental effects than Category A projects and is usually site-specific. Few, if any, of its effects are irreversible and, in most cases, mitigation measures can be designed more readily.</p> <p>Category C. The project is likely to have minimal or no adverse environmental effects.</p>
Information requirements	<p>EDC reviews environmental information provided by the project sponsors. The required documentation varies according to the project's categorization.</p> <p>Category A. The project normally requires an Environmental Impact Assessment report. (Annex 3 of the Directive lists the required contents of the report.)</p> <p>Category B. The project requires less information (the amount varies according to the project).</p> <p>Category C. The project generally does not require an environmental assessment.</p>
Evaluation	At a minimum, the project must comply with host country standards. For category A or B projects, EDC uses the international standards it determines are most appropriate.
Determination	<p>EDC must determine whether</p> <ul style="list-style-type: none"> • a project is likely to have adverse environmental effects regardless of mitigation measures; • it is justified in entering into the transaction, despite these effects. <p>The Directive sets out grounds for justification. Category A and B projects, located in Canada or the United States that meet host country environmental requirements, and Category C projects do not require determination.</p> <p>EDC will decline a project if it cannot</p> <ul style="list-style-type: none"> • obtain sufficient information to conduct an environmental review of the project; • justify supporting a project with adverse environmental effects, despite mitigation measures; and • obtain the necessary covenants or monitoring rights.
Covenants and monitoring	EDC negotiates financial agreements to include appropriate covenants, warranties, and monitoring provisions.

*Special drawing rights—an artificial currency unit defined as a basket of national currencies established by the International Monetary Fund.

Source: Based on EDC's Environmental Review Directive

26. When does the Directive apply? The Directive only applies to a small percentage of EDC's business volume—1.2 percent in 2003 (Exhibit 4). First, it only applies to project-related transactions. In 2003, project-related transactions represented less than 1.5 percent of EDC's business volume. However, the Directive only covers those transactions with a repayment term or coverage period of two years or more. This project focus and two-year threshold exclude EDC's short-term accounts receivable insurance, which in 2003 represented approximately 70 percent of its business volume. This exclusion is common business practice in all export credit agencies we reviewed.

Exhibit 4 The Directive applies to a small percentage of EDC's \$51.9 billion business volume, 2003



Source: Export Development Canada

Terms used in EDC's Environmental Review Directive

Equity transaction—The acquisition by EDC of an interest in an entity, other than by way of the taking or realization of security.

Financing transaction—Can include a loan, a purchase of receivables, a lease, or a financing guarantee entered into by EDC.

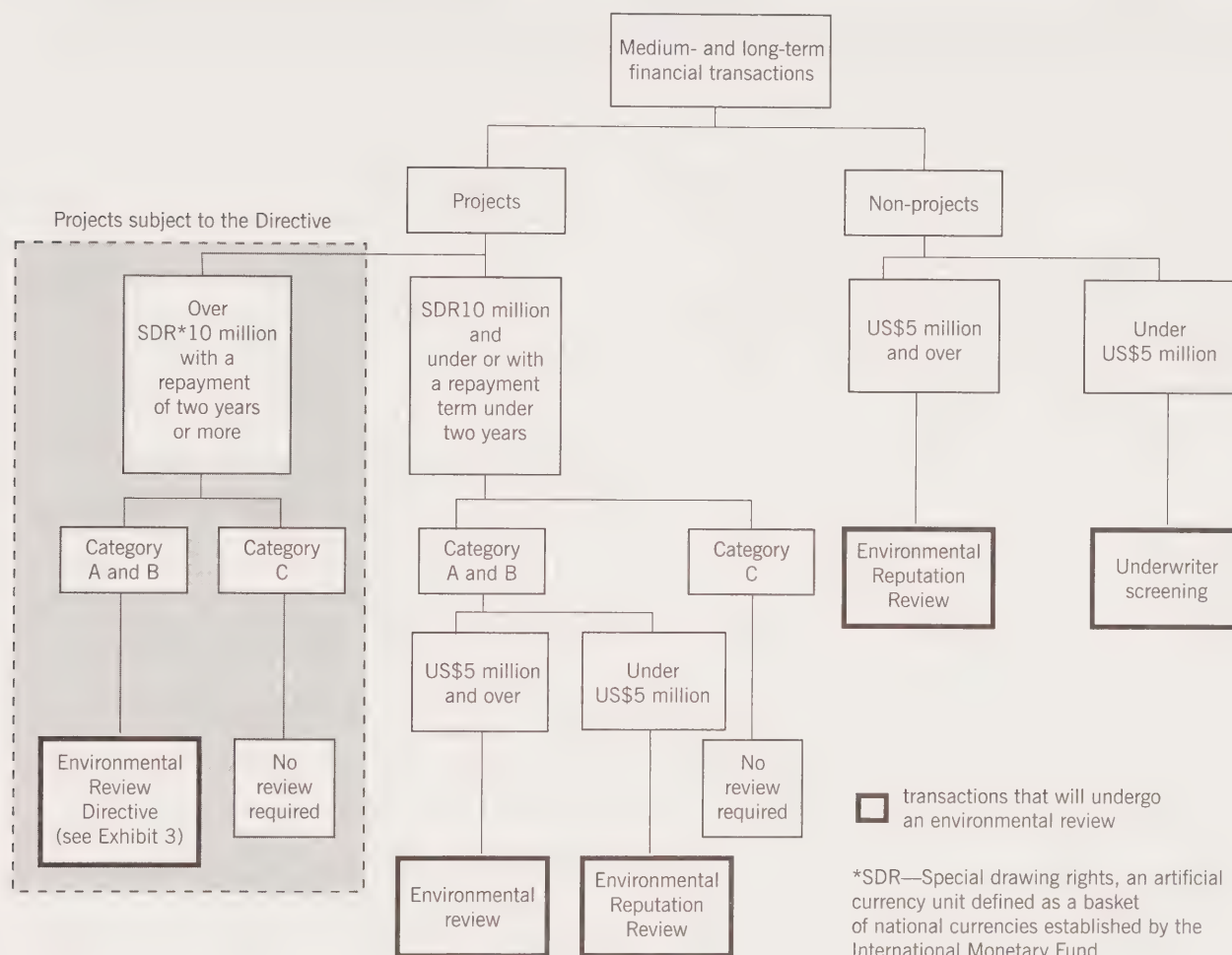
Political risk insurance transaction—Insurance coverage to protect against political risks such as foreign exchange transfer difficulties, expropriation by a host government, or war, revolution, and insurrection.

SDR—Special drawing rights, which is an artificial currency unit defined as a basket of national currencies established by the International Monetary Fund.

27. Second, the Directive applies to those medium- and long-term financial services that are **financing, political risk insurance, or equity transactions**. This excludes contract and insurance bonding. The scope of the Directive narrows this further to support for project-related transactions with a value greater than **SDR10 million**, which is the equivalent of about C\$20 million.

28. In the first two years of its operation, the Directive applied to eight completed project-related transactions per year. EDC's remaining project-related transactions are covered by the processes described below.

29. Other environmental review processes. EDC extends its environmental risk management beyond the scope of the Directive to three supplemental review process streams. No public document describes these processes. Rather, EDC relies on its internal corporate manual on environmental review practices to guide application of its supplemental reviews. Together, the Directive and the supplemental review processes form a complex system for determining which transactions will be subject to environmental review (Exhibit 5).

Exhibit 5 How EDC determines what transactions undergo an environmental review

Source: Adapted from EDC's Environmental Review Process Manual

30. The first supplemental process deals with project-related transactions that are less than the Directive's monetary threshold but over US\$5 million. EDC subjects higher risk projects in this review stream to a categorization and review process similar to the one it conducts under the Directive.

31. The second process is an environmental reputation review. EDC applies this to higher risk project-related transactions below the US\$5 million threshold as well as to non-project transactions above US\$5 million. EDC establishes an environmental reputation risk rating by assessing various factors, including country, sector of activity, size of operations, site characteristics, and the environmental policies and track record of the company involved.

32. The third process screens non-project related transactions below US\$5 million for environmental risks. Financial service managers and

underwriters carry out this type of screening. EDC's Environmental Advisory Services group oversees the application of the Directive and the first two supplemental processes.

33. Case Studies. EDC publishes only limited information about its environmental reviews, primarily with respect to its higher risk (Category A) project transactions. The six case studies in Exhibit 6 help illustrate the application of EDC's Directive and other environmental review processes. They include examples of signed and declined transactions. We omitted names of parties, exact geographic locations, and, in certain cases, the precise international standards applied to comply with EDC's disclosure policy.

Focus of the audit

34. The *Export Development Act*. The Act mandates the Auditor General of Canada to audit the design and implementation of EDC's Environmental Review Directive on a regular basis and to submit her report to the board of directors of EDC, the Minister of International Trade and to both houses of Parliament. At the request of the Minister of International Trade, we undertook this audit two years after implementation of EDC's new Directive and other environmental review processes.

35. In conducting our audit, we identified key elements of a suitably designed environmental review process similar to those used for our 2001 Report. These elements are based on a comparative review of the documented policies of international financial institutions, including export credit agencies, private sector commercial banks, and multilateral development banks. We compared them with EDC's Environmental Review Directive and other environmental review processes.

36. We assessed whether EDC was applying its Environmental Review Directive and other environmental review processes as designed and reviewed the manner in which EDC responded to the recommendations in our 2001 Report. Further details about our scope and approach can be found in **About the Audit** at the end of this Report.

Observations and Recommendations

Design suitable for a financial institution

The Environmental Review Directive has most elements of a suitably designed environmental review policy

37. Our comparative review of the policies of export credit agencies, private sector commercial banks, and multilateral development banks identified key elements of an environmental review policy suitable for an international financial institution (Exhibit 7). We found that EDC's current environmental review processes include most (34 of 37) of the elements included in the policies of a majority of the institutions we reviewed. These are referred to as standard elements. The Directive meets more standard elements than EDC's previous policy. While designed to be in line with the OECD Common Approaches, the Directive also includes one element that is not yet common

Exhibit 6 How EDC applies the Environmental Review Directive and other environmental review processes

Signed Transactions

Environmental Review Directive (Category A project)

Project description. EDC was asked to provide political risk insurance for the development and operation of an open-pit gold mine on a greenfield site in South America.

Issues. The project is located in a rainforest with discontinuous sections of savanna and savanna forest along the central section of the mining concession. Small-scale mining was previously carried out on the site. Environmental assessment reports identified potential impacts on vegetation, wildlife and water resources, and the socio-economic environment. The mining plan did not require resettlement of the population.

Review process. EDC reviewed the project sponsor's environmental and social impact assessment reports, as well as a review of the reports by a third party. In its review, EDC used World Bank Group standards to benchmark the project's design; it requested and received clarification and further information on project design and operation. EDC also visited the site and met with members of the community to hear their concerns on the project. EDC determined that the project was designed to meet or exceed internationally recognized good practices, guidelines, or standards and that its potential adverse effects, taking into account mitigation measures, were not significant. EDC requires annual monitoring reports on the project.

Environmental Review Directive (Category B project)

Project description. EDC was asked to provide financing for the construction of an aqueduct in the Caribbean.

Issues. EDC identified several issues including competing resource needs for drinking water and agricultural use and the impact on aquatic life in the source river.

Review process. EDC reviewed an environmental impact assessment study commissioned by the client as well as a supplemental environmental report prepared by the environmental division of the Canadian firm contracted to build the aqueduct and used the World Health Organization Guidelines for Drinking Water Quality as the appropriate standard. EDC later requested additional information on the project's design and operational phase. Loan disbursement was conditional on receiving the additional information.

Supplemental environmental review process (Category A project)

Project description. EDC was asked to provide political risk insurance for the design and construction of a solid waste landfill facility in South America.

Issues. EDC identified several issues: emissions of greenhouse gases, loss of vegetation, and potential contamination of underground water. Mitigation measures have been introduced to reduce any potential impacts.

Review process. EDC reviewed an environmental assessment report prepared by a firm registered with the country's Ministry of Environment and Renewable Natural Resources. It benchmarked the project's design against World Bank Group standards and found no significant adverse gaps. EDC believes the project will improve the baseline conditions of the area and will produce a net environmental and social benefit.

Environmental reputation review process (non-project transaction)

Transaction description. EDC was asked by a Canadian company to renew reinsurance coverage for a reclamation bond to ensure availability of funds for land reclamation of a coal mine in North America.

Issues. EDC used United States standards to examine the potential risk to its reputation that could result from the company's coal-mining and power generating operations. This included the effects of emissions on a protected area located about 50 kilometres from the plant.

Review process. EDC used its environmental reputation risk process to review the environmental track record of the company as well as the compliance history of the coal mine and the coal-fired power plant. EDC concluded that the risk was acceptable.

Exhibit 6 How EDC applies the Environmental Review Directive and other environmental review processes (Continued)

Declined Transactions	
<p>Underwriter screening process</p> <p>Transaction description. EDC was asked to provide contract insurance and bonding support for consulting services for a pipeline project in South America.</p> <p>Issues. The pipeline route crossed several ecologically sensitive areas and required resettlement of local communities.</p> <p>Review process. EDC reviewed a previous request for support for the same project that it had declined. In its initial review, EDC had concluded that the project was likely to have significant adverse environmental impacts that might be diverse and irreversible. In some instances, the project did not comply with the World Bank's Pollution Prevention and Abatement Handbook measures on oil and gas developments. EDC declined support for this transaction again. Maintaining a declined project list streamlines the review process.</p>	<p>Environmental Review Directive (Category A project)</p> <p>Project description. EDC was asked to provide financing for the development of a newsprint mill on a greenfield site in Asia.</p> <p>Issues. Potential issues included air emission impacts, ambient air quality, noise, and thermal impacts of effluent discharges.</p> <p>Review process. EDC selected World Bank and European Economic Community environmental standards as appropriate international standards for reviewing the plant. During its review, EDC noted information gaps regarding the technology to be used to address potential impacts. There was also a lack of clarity on the public consultation process. EDC declined support for the project; it could not confirm to its satisfaction that the selected environmental performance standards would be met.</p>

practice for export credit agencies: requiring third party review of environmental impact assessment reports.

38. The Directive omits three standard elements: ensuring due regard for international environmental agreements, co-ordination of review efforts with other financial institutions, and notification of stakeholders for public consultation. In our file review, we did find evidence that, in practice, EDC takes international environmental agreements into consideration and co-ordinates its review efforts with other financial institutions. Public consultation is addressed later in the Report.

39. **Missing policy elements.** Notwithstanding EDC's attention, in practice, to international environmental agreements, in our view a Crown corporation that implements Canadian government policy should explicitly state its commitment to take into account Canada's international environmental obligations. Most financial institutions in our comparative review now take into account international environmental agreements as a standard element of their environmental review policy. EDC is among the export credit agencies that do not have this policy element.

40. **Recommendation.** EDC's environmental review policies should include a requirement that EDC take into account Canada's international environmental commitments when considering support for projects.

EDC's response. EDC believes that taking Canada's international environmental commitments into account is an important aspect of its environmental review processes and is pleased that the Office of the Auditor General has recognized our current practices in this regard. EDC will respond to this recommendation by working with the appropriate government department(s) to increase the exchange of information and identify the international environmental agreements relevant to EDC's environmental reviews and establish a commitment within our policies reflecting this practice.

Exhibit 7 Elements of an environmental review process for an international financial institution

Main element		Sub-elements	Category
General features	Documented environmental and social review process appropriate to the organization's mandate	Demonstrate that an environmental and social scan of the mandate has been undertaken (such as an assessment, minutes of management meetings)	Standard ¹
		List key objectives of the process	Standard
		Define key terms used in the process (such as project, environment, environmental risk, and environmental effect)	Emerging ²
		Demonstrate management commitment (such as a public statement on process, a management review process)	Standard
		Demonstrate management accountability (such as a designated management representative responsible for decisions under the process)	Standard
		Demonstrate organizational capacity to implement the process (such as trained staff and resources)	Standard
		Provide for monitoring of process conformance	Standard
		Provide for public reporting on the nature and extent of the application of the process	Standard
		Include a policy commitment and procedures to promote continual learning and improvement in the organization and to inform clients of changing requirements	Standard
Review of financial services applications	Systematic procedures for financial services applications	Provide objective criteria and/or procedures for	
		• classifying all applications by environmental risk regardless of level of financial involvement	Emerging
		• determining significance of environmental risks	Standard
		• exempting applications from review	Standard
		• refusing support	Standard
		• special categories such as modifications, expansions, or maintenance	Standard
		• applications that might affect sensitive ecosystems and protected areas	Standard
		Require third-party review (at arm's length) of the client's environmental assessment, where the financial institution's process has determined the potential for significant environmental risks	Emerging
		Include tools for process implementation (such as guidelines for clients, training packages for internal staff)	Standard

¹ Standard elements are included in the procedures of the majority of the institutions that we examined.² Emerging elements reflect the process of only a minority of the institutions that we examined.

Exhibit 7 Elements of an environmental review process for an international financial institution (Continued)

	Main element	Sub-elements	Category
Contents of environmental assessment reports	Specification of the expected contents of environmental assessment reports	Describe the surrounding environment	Standard
		Describe the intended use of funds or financial support and any related physical structures	Standard
		Describe host country laws, regulations, standards, and other applicable environmental requirements	Standard
		Assess and describe known and potential environmental risks (for example to air, water, land, protected areas)	Standard
		Identify mitigation measures and monitoring required	Standard
		Identify residual impacts after mitigation	Standard
		Prepare an analysis that justifies accepting residual impacts	Standard
		Describe emergency response procedures where there is a significant potential impact on the environment in the case of an incident	Emerging
		Identify and assess public and stakeholder concerns	Standard
		Consider alternatives to the undertaking	Standard
		Consider cumulative effects	Emerging
Environmental and social standards	Documented policy and procedures respecting environmental and social standards	Comply with host country regulations and standards	Standard
		Apply international environmental standards and guidelines (such as World Bank Group's standards, ISO 14000, or a numeric standard such as the World Health Organization's air quality guidelines)	Standard
		Apply home country standards in the absence of host country or international standards	Emerging
		Ensure due regard for global environmental agreements and conventions (such as Convention on Climate Change, Kyoto Protocol, Montreal Protocol, Convention on Biodiversity, Convention on Environmental Impact in a Transboundary Context, Aarhus Convention)	Standard
Co-operation among institutions	Documented policy and procedures for co-operation	Co-ordinate environmental review and monitor efforts when more than one financial institution is involved (for example, co-financing)	Standard
		Allow flexibility to use existing environmental assessments	Standard
Disclosure	Documented policy and procedures for active disclosure	Define information to be disclosed, by whom and when	Standard
		Establish a format for public disclosure of environmental assessment findings	Standard

Exhibit 7 Elements of an environmental review process for an international financial institution (Continued)

Main element		Sub-elements	Category
Public consultation	Documented policy and procedures for public consultation	Determine the need for public consultation	Standard
		Identify relevant stakeholders	Emerging
		Notify stakeholders	Standard
		Receive and summarize public consultation results	Standard
		Document gaps in consultation (for example, where consultation was not possible for cultural or political reasons)	Emerging
		Disclose results of public consultations	Standard
Environmental covenants	Documented procedures that establish and include environmental covenants in contractual agreements	Document any changes or covenants imposed on the application as a result of internal policies, environmental assessment, and public consultations	Emerging
		Monitor and report on compliance with the covenants by the client or a third party	Standard
		State the applicant's obligation to take corrective action if monitoring indicates a problem	Emerging
Supervision and monitoring	Documented procedures to define how transactions are to be supervised and monitored by the institution and to ensure compliance with established covenants	Arrange occasional inspections by the institution or a local agent to verify compliance reports	Standard
		Establish follow-up procedures where non-compliance has been identified	Standard

41. EDC's Directive eliminated two elements found in its former policy: emergency response procedures and the need to consider cumulative effects. This occurred when EDC substituted the list of elements required for an environmental impact assessment report used in the OECD Common Approaches for what it previously used. We consider this approach to be a step backward for EDC. In our view, EDC should not eliminate elements from its environmental review policy to conform to a level playing field.

The Environmental Review Directive's narrow scope

42. **Objective.** Our 2001 Report recommended that EDC clarify the objective of its Environmental Review Framework. EDC responded by identifying the purpose of the Directive as establishing the process required to make a determination regarding EDC's justification in entering into transactions. This objective restates EDC's legal obligation to carry out environmental reviews. It is framed in terms of legal risk rather than, as

suggested in our 2001 Report, the intended results of an environmental review—namely that the projects EDC approves are environmentally sound and sustainable

43. Environmental review policies generally contain statements of objectives or purpose intended to guide their application and interpretation. For example, the OECD Common Approaches is based on principles that include the promotion of good environmental practices and consistent processes with a view to achieving a high level of environmental protection. EDC's environmental review policies are not governed by any similar over-arching principle. We believe that EDC, as a Crown corporation, should frame its objectives for environmental review based on principles of environmental protection and sustainability. Such principles serve to complement its legal objective.

44. Recommendation. EDC should amend its Directive and other policies to establish general principles to guide its interpretation and application with a view to supporting projects that are environmentally sound and sustainable.

EDC's response. EDC believes that general principles can be useful in guiding the interpretation and application of environmental review policies and practices. EDC has already taken this approach in establishing an environmental commitment in its Code of Business Ethics and by identifying the environment as a key pillar of EDC's Statement of Commitment on Corporate Social Responsibility. In light of this recommendation, EDC will consider amending the Environmental Review Directive and other policies to incorporate the principles underlying this environmental commitment.

45. Exclusion of short-term transactions. The Directive and other review processes do not apply to short-term accounts receivable insurance. Although noting this exclusion is a practice common to many export credit agencies, our 2001 Report recommended that EDC conduct an environmental risk analysis to determine whether such exclusion is justified. It has not done so.

46. Recommendation. EDC should conduct a risk analysis to determine what risks, if any, it is open to by excluding short-term insurance from environmental review.

EDC's response. In response to the 2001 audit recommendation on the exclusion of EDC's short-term business from the former Environmental Review Framework, EDC conducted an analysis of its short-term business portfolio which considered the business and environmental considerations related to this exclusion from environmental review. The Corporation will consider a further elaboration of this analysis. As a further mitigating effort, EDC has provided training to all short-term insurance underwriters to improve their ability to identify situations that may require guidance, and they are encouraged to contact the Environmental Advisory Services Group to discuss any environmental concerns arising from the short-term business transactions they encounter.

47. Other coverage restrictions. The Directive clearly states that its environmental review procedures apply only to transactions related to a project. The Directive defines a project as a physical development that is

Greenfield—A site on which there is no previous development.

industrial, commercial, or infrastructure-related on a **greenfield** site or a facility undergoing major extension or modification. Additional definitions in the Directive further narrow its application to project-related transactions where EDC or the exporter is dealing with persons in a position to influence the design and direction of a project. The Directive does not apply to the establishment of corporate loan facilities, such as lines of credit, where there is no identified project; however, it applies if a client requests an advance under a line of credit for a particular project.

48. Although its enabling legislation allows EDC discretion to establish definitions for its Directive, it has chosen some criteria in these definitions that are based on factors other than potential environmental risk. Notions of ownership, control, and influence are not indicators of risk.

49. **Monetary thresholds.** The Directive sorts transactions according to their monetary value. However, a monetary threshold is not an indicator of environmental risk. Since our 2001 Report, most of the export credit agencies we reviewed have adopted some form of thresholds. EDC uses the same threshold that the OECD Common Approaches recommends.

50. The OECD Common Approaches applies no financial thresholds when it considers projects in sensitive areas (defined as including parks, protected areas, and wetlands). EDC plans to bring its review policy for sensitive areas into line with OECD policy. Projects in sensitive areas would be subject to EDC's first supplemental environmental review process, as described earlier.

51. **Project splitting** During the consultation period on the Directive, civil society groups raised concerns that applicants would split projects to avoid a monetary threshold that would otherwise subject projects to a detailed environmental review. We found no evidence of project splitting in our audit work.

52. **Increased burden for supplementary review processes.** The Directive's restrictions narrow its scope to the point that it captured eight completed project-related transactions per year since its adoption. This increases the burden on the supplementary environmental review processes to ensure that risks are identified and properly assessed in cases where a full environmental impact assessment may not be otherwise warranted. For example, transactions that don't qualify under the Directive may nonetheless involve activity with potential adverse environmental impacts. In such cases, even a minor contribution to an environmentally unsound operation has the potential to cause severe reputation damage to EDC and to reflect negatively on the Government of Canada.

53. EDC has chosen to manage the environmental risks associated with its mandate to promote trade by focussing much of its environmental review efforts on project-related transactions. However, it also established a procedure for environmental reputation reviews for non-project transactions.

54. There is no standard practice among financial institutions for conducting environmental reputation reviews. It remains a highly subjective exercise. As this area evolves, EDC needs to update its methods to apply objective,

practical criteria to ensure that its environmental reputation reviews are working effectively.

Implemented as designed

Major improvements in implementation

55. We reviewed whether EDC implements its environmental review processes as designed. In doing so, we looked at how EDC's processes meet key design elements, including the steps set out in the Directive.

56. In our 2001 audit of EDC's previous Environmental Review Framework, we found significant differences between the Framework's design and its operation. We reported finding gaps at each stage of the environmental review process and we concluded that the Framework was not operating effectively.

57. In our current audit, we found that EDC has made major improvements to the way it implements its environmental review processes, including the Directive. Overall, we found that the Directive operated as designed. When we compared implementation against the design elements of the Directive, we generally found that EDC

- screened and categorized transactions appropriately;
- reviewed environmental assessment reports or other information. EDC requested additional information when warranted and, in certain instances, made filling information gaps a requirement of financing;
- identified which international standards to apply;
- based decisions to support transactions on sufficient information. EDC declined support when adequate information was unavailable;
- took decisions at the appropriate level of authority; and
- included environmental covenants and monitoring requirements in transaction documentation when appropriate.

58. We found that EDC generally applied its other environmental review processes, including its review of projects not subject to the Directive and its environmental reputation review process, in accordance with its internal procedures manual.

59. Applying EDC's Directive and other review processes has been a learning experience for EDC staff and clients. EDC clients interviewed by us confirmed that EDC staff were very professional in dealing with issues that arose during the review process. There was also general consensus that the Directive neither imposed an undue financial burden nor caused unexpected delays in processing transactions.

Internal procedures and accountability

60. Our 2001 Report recommended a more systematic approach to review processes. Our current audit found that EDC made significant improvements in staff training and in strengthening its own control systems.

61. **Staff are trained in the new processes.** EDC went to considerable effort to hire experienced staff. It hired a senior environmental specialist who supervises the six-member team that applies the Directive and other environmental review processes. It organized extensive staff training after the

new Directive came into effect and trains all new employees on the environmental review processes.

62. Monitoring procedures. In 2001, we reported finding limited evidence of systematic monitoring of transactions. EDC has since developed new internal procedures and systems to ensure appropriate monitoring. Staff track reporting requirements on an automated system and follow new procedures to verify late or incomplete reports or incidences of non-compliance. EDC's environmental specialists assess these reports.

63. In the transactions with monitoring requirements we reviewed, we found that EDC followed its internal procedures. When monitoring reports were late, EDC followed up to ensure that they would be provided. When EDC found non-compliance with negotiated environmental covenants, staff requested further information on the problems and the actions taken to rectify the non-compliance. EDC's ability to carry out effective monitoring is constrained in those transactions where it is one of many lenders in a loan syndicate.

64. Enhanced mechanisms to improve supervision. Since our 2001 audit, EDC strengthened its accountability mechanisms to monitor all environmental review processes. These mechanisms include the following:

- an automated system for tracking medium- and long-term transactions that uses a series of check points to ensure that transactions follow all required environmental review steps;
- an Environmental Advisory Services team that reviews the environmental impacts of project and non-project transactions;
- internal audits of how staff use EDC's automated transaction system and its disclosure policy. The audits identify process deficiencies and recommend measures to correct them;
- enhanced approval levels appropriate to the size of the transaction to ensure that required opinions and other documentation have been obtained;
- the Audit Committee of the Board of Directors overseeing issues to do with the Directive and the disclosure policy; and
- a Compliance Officer whose mandate is to provide additional assurance to the public that EDC is complying with its policies on transparency and disclosure, environmental review, human rights, and business ethics (see case study, EDC's compliance officer mechanism: The first test).

EDC has broad discretion in applying the Directive

65. Discretion. The legally binding nature of the Directive influenced its design. EDC was concerned that a legal obligation to carry out environmental reviews would open up its decisions to judicial review, so it used the broad discretion given to it under the *Export Development Act* to restrict the scope of the Directive's application and to build a considerable amount of flexibility into its design. The policies of other export credit agencies we reviewed also provide for discretion in their application.

EDC's compliance officer mechanism: The first test

January 2002: EDC appointed its first Compliance Officer. This ombudsman-like position serves to enhance accountability. EDC's Compliance Officer receives complaints on policies and initiatives about transparency and disclosure of information, environmental reviews, human rights, and business ethics. Any interested person, including clients and non-governmental organizations, can submit a complaint.

July 2003: The Compliance Officer received the first complaint falling under her mandate. The complaint, filed by a non-governmental organization, concerns EDC's support for the construction of a second CANDU 6 nuclear reactor on the site of an existing nuclear power plant in Cernavoda, Romania. The complaint alleged that by approving the transaction, EDC violated the "spirit" of its disclosure policy, its Environmental Review Directive, and its Code of Business Ethics. It also alleged that EDC violated provisions of the Directive by not

- disclosing an environmental impact assessment report (EDC disclosed only a summary report);
- providing sufficient information; and
- complying with host country requirements and international standards.

October 2003: The Compliance Officer investigated and reported to the complainant that she found no clear evidence of non-compliance. She indicated that she would recommend an internal audit of compliance with all three policies. EDC's Internal Audit and Evaluation conducted this audit in two phases.

May 2004: The Compliance Officer reported to the complainant that EDC's internal compliance audit concluded that EDC had complied with all relevant policy sections of its Code of Business Ethics and Disclosure Policy.

June 2004: The Compliance Officer reported that the second internal audit found that EDC "satisfactorily complied with all relevant policy sections of the Environmental Review Directive that were identified by the complainant."

We reviewed EDC's files on the Cernavoda transaction during the course of our audit and concluded that EDC had complied with the process set out in its Environmental Review Directive. EDC's Directive is designed to give it broad discretion in its application. This discretion allows EDC to exercise its professional judgment to define compliance in a variety of circumstances. The public cannot evaluate compliance since it does not know which of the range of possible options EDC has considered or the one it has chosen to comply with.

We expect that EDC's treatment of future complaints will be carried out in a more timely fashion, consistent with that part of its Code of Business Ethics that states that EDC's corporate policy is that communications "be truthful and transparent in a way that will withstand the highest degree of public scrutiny."

66. This discretion allows EDC to exercise professional judgment at various steps in the application of the Directive:

- categorizing projects,
- analyzing environmental impact assessment reports to determine what information is required and whether information gaps are justified,
- selecting which international standards to use,
- determining the significance of environmental impacts, and
- determining justifications for entering into transactions.

67. We are satisfied that EDC takes care in exercising its professional judgment to categorize transactions and make determinations on higher risk projects. At the same time, we noted areas for improvement in documenting how EDC exercises this discretion: analysis of environmental impact assessment reports and public consultations.

68. Contents of environmental impact assessment reports. The Directive establishes different information requirements and formats for environmental impact assessment data in accordance with the risk category of a project. Annex 3 of the Directive lists the aspects normally covered by environmental impact assessment reports for higher risk projects. But the Annex also notes that every element need not be covered for the report to be complete. Still, EDC needs to carefully consider relying on reports that don't cover every element and should consistently document those cases where it decides to do so. Although it did address in some form gaps it identified in environmental impact assessment information provided, EDC's documentation in some cases was weak.

69. Recommendation. EDC should ensure that it adequately documents the circumstances that justify its decision to accept information gaps in environmental impact assessment reports in its environmental review of project-related transactions.

***EDC's response.** EDC views any material gaps in environmental impact assessment information very seriously and has refused to support projects on this basis (as outlined in EDC's Chief Environmental Advisor's Annual report and in this Report). EDC believes that all information gaps in environmental impact assessment reports should be documented and the decisions to accept these gaps need to be justified. It is standard practice for all Environmental Advisory Services project opinions to address Environmental Impact Assessment elements and, if elements are not fully addressed, to note justifications where appropriate. EDC will review the consistency of its documentation of this aspect and will make modifications as appropriate.*

70. Public Consultation. Public consultation under the Directive is discretionary. The Directive states that EDC "expects," rather than requires, public consultation on Category A projects. This matches the OECD Common Approaches and the practices of many other export credit agencies. The Directive builds in additional flexibility for the public consultation elements by allowing for adaptation to the various political, cultural, and legal contexts in the countries where EDC carries on business. Like its export credit agency counterparts, EDC does not explicitly define the type of public consultation expected.

71. However, multilateral banks, such as the International Finance Corporation, require consultation for Category A projects. These institutions use public consultation to identify and resolve potential problems early on by bringing additional expertise, information, and viewpoints into the project process. There is no standard methodology for public consultations. But the International Finance Corporation prepared a guidance document, *Doing*

Better Business through Effective Public Consultation and Disclosure. It believes that “consulting with the public makes good business sense.”

72. EDC could use this guidance to help accomplish the basic purpose of public consultation, namely to identify and consider the concerns of affected people in the host country. The policies of some international financial institutions, including that of EDC, require, at a minimum, compliance with the public consultation requirements of the host country. There may, however, be situations where going beyond a strict adherence to legal requirements is warranted to adequately manage environmental risk and reputation issues.

73. We found EDC’s assessment of the adequacy of public consultation was not consistent. EDC did not always receive sufficient information to determine the adequacy of the consultation. Nor was it always clear from available documentation what influence, if any, consultation had on the projects. A more recent transaction reviewed by us indicated that EDC exercised greater due diligence about the nature and extent of host country requirements on public consultation.

74. In some instances, EDC’s clients become involved in a project after consultation has taken place and may not have access to public consultation records. In other cases, circumstances regarding the host country culture and laws or the nature of the project itself may lead EDC to support a transaction without full information on public consultation. However, in all circumstances justification for proceeding without full information on public consultation needs to be fully documented in the files. We did not always find this to be the case.

75. Our audit found that EDC did not meet the standard design element for notification about public consultation. Although the policies of a majority of the export credit agencies we reviewed included this element, the OECD Common Approaches does not. There is no uniform practice for public consultation notification among export credit agencies because it is the project sponsors, not the agencies, that carry out this consultation. In our view, EDC’s policies should encourage appropriate notification for public consultations in the projects they support.

76. **Recommendation.** EDC should be diligent in confirming that public consultations are, at a minimum, in accordance with the requirements of the host country. In cases where EDC decides to proceed with a transaction despite the absence of full information on public consultation, EDC should document its justification for that decision. Where warranted, EDC should go beyond a strict adherence to host country public consultation requirements, in order to adequately manage environmental risk and reputation issues.

EDC’s response. EDC’s *Environmental Review Directive* requires compliance with host country requirements as per Paragraph 22 of the Directive which states “the project in respect of which EDC is conducting a review has been designed to comply with host country environmental requirements, such as any applicable provisions for local consultation...” Where information related to public

consultations is not comprehensive, EDC carefully considers whether the absence of this information is a key concern with respect to the support of the project. EDC will review the consistency of its documentation of this aspect and will make modifications as appropriate.

77. Transparency. The discretion built into the different stages of application of EDC's environmental review processes makes it difficult for Parliament and the public to understand how EDC applied, interpreted, and oversaw its environmental reviews. In our view, the counterbalance to this discretion is greater transparency.

78. Without greater transparency, Parliament and Canadians lack information about what impact, if any, EDC's environmental review processes have had to ensure that EDC upholds high standards of environmental protection and sustainable development. Internal controls and safeguards alone do not provide this assurance to the public. EDC needs to demonstrate that its exercise of discretion under its environmental review policies upholds these high standards. Our comments below discuss steps EDC could take to enhance transparency.

Other observations

Disclosure is an essential element for a credible environmental review process

79. EDC acknowledges that disclosure of environmental information is emerging as an essential element of a credible environmental review process. Prior disclosure of information for projects with potentially significant environmental impacts (Category A projects) has, in recent years, become a regular policy in most export credit agencies we reviewed. It allows important information to be brought forward from other sources and taken into consideration in project review. In EDC's case, the information disclosed both prior to and after signing a transaction needs to enhance public trust in the manner in which it carries out its legislated duty to conduct environmental reviews.

80. Since our 2001 Report, EDC has developed a disclosure policy (www.edc.ca/corpinfo/csr/disclosure/disclosure_policy_e.pdf) that includes EDC's commitment to disclose, with client consent, that it is considering support for a Category A project under its Directive.

81. EDC discloses environmental and individual transaction information on a voluntary basis with the consent of its clients. It is not legally obliged to provide information under access to information legislation. Nor does EDC's current disclosure policy fall under the same legal obligation as its Directive.

82. EDC must balance commercial competitiveness and client confidentiality with its need to demonstrate accountability and assure public confidence in the execution of its mandate. These considerations led EDC to include the following information for release under its prior disclosure policy: date of posting, country of the transaction, a general description of the project, the project name, the project sponsor, and the project contact.

83. EDC also took its client concerns about competitiveness into account and did not make consent for prior disclosure a precondition for EDC

support. However, at the time it consulted on its draft policy, there was no information on the number of transactions to which this policy would apply.

84. To date, EDC has experienced few problems obtaining consent to disclose what has amounted to minimal information. From the time it came into effect until 31 December 2003, the prior disclosure policy has applied to eight completed Category A projects. Clients granted consent for disclosure in seven of those projects. EDC officials informed us that they received comments from the public on only one of those disclosures.

85. In our view, EDC needs to consider taking a leadership position in making prior disclosure a precondition of EDC support. This would demonstrate a greater commitment to transparency with limited effect on competitiveness in the few transactions to which it applies.

86. **Additional disclosure.** EDC released its first annual Chief Environmental Advisor's report on its Web site in September 2003 (www.edc.ca/corpinfo/CSR/environment/index_e.html). This report covers projects reviewed during 2002 and includes information on

- the number of projects in each category,
- the number of signed projects in each sector and in each region,
- the name and location of signed Category A projects, and
- whether EDC refused project proposals on environmental grounds during the same period.

This report provides information in addition to what EDC discloses under its policy. This initiative shows promise for greater commitment to transparency in EDC disclosure.

87. **International standards.** EDC responded to our 2001 recommendation to identify the standards it uses in its review of projects. Annex 5 of the Directive lists examples of internationally recognized good practices, standards, and guidelines to use as benchmarks in reviewing projects. The list gives EDC the flexibility to select the standard most appropriate for any project.

88. EDC does not disclose the standard that it uses for any particular project. Revealing the specific international standard upon which it has based its determination would give the public and Parliament a greater measure of confidence that EDC is applying appropriate standards when it supports exports.

89. At the time EDC adopted the prior disclosure component of its policy, it agreed to amend its individual transaction reporting to refer to the international standards that were met or exceeded for Category A projects. It did so by referring to the catalogue of standards from its "Illustrative list of internationally recognized good practices, standards and guidelines" (Annex 5 of the Directive). This list adds no new information to its disclosure efforts and does not identify the specific standards it has used in carrying out its environmental review for those projects.

90. **Recommendation** EDC should disclose the specific standards it used in carrying out its environmental review of Category A projects.

91. Evolving disclosure practices. EDC has undertaken to amend its disclosure policy as practices of other credit agencies evolve. We have noted the following enhanced disclosure practices among the agencies we reviewed:

- **Prior notice period**—The period for advance disclosure for export credit agencies varies from none to 45 days. This contrasts with 60 to 120 days for multilateral development banks. The OECD Common Approaches recommends that its members should seek to disclose environmental information about a Category A project 30 days before commitment.
- **Information disclosed after signing**—Some export credit agencies enhance transparency by releasing additional information on environmental reviews of projects after signing. This information can include
 - the standards used for evaluating high-risk projects;
 - a list of signed projects with their environmental categorization, published on a yearly or quarterly basis; and
 - reference to the mitigation measures and monitoring requirements for signed projects.

92. EDC is considering revisions to its prior disclosure policy to align with the OECD 30-day period. In our view, EDC needs to consider at the same time whether it wishes to keep pace in making other transparency enhancements to its policy.

93. Recommendation. EDC should amend its disclosure policy and practices to take into account evolving best practices and to enhance corporate transparency by

- at a minimum, reflecting the 30-day prior disclosure recommended in the OECD Common Approaches;
- listing all signed projects with their environmental categorization on a yearly basis; and
- indicating whether mitigation measures or monitoring requirements were imposed.

EDC's response to the recommendations in paragraphs 90 and 93. EDC ensures that it operates in accordance with the OECD Common Approaches and, as such, is already applying the 30-day prior disclosure provision recently added to the OECD's Common Approaches agreement. It is important to note that EDC was part of the initial group of export credit agencies that developed an ex-ante disclosure policy, and that EDC continues to support the inclusion of this element at the OECD level.

EDC will address the further recommendations by considering appropriate enhancements to the Chief Environmental Advisor's Annual Report among its options.

Project-related social impacts

94. The Directive looks at one aspect of social impacts: project-related social impacts. The Directive defines this as “any instance of involuntary

resettlement or any other adverse change that the project imposes on indigenous or vulnerable groups or on cultural heritage.” The Directive is not designed to address broader social aspects such as human rights and labour conventions. This is consistent with the approach of other export credit agencies.

95. The review of project-related social impacts under the Directive helps protect EDC’s reputation from serious damage by guiding it away from supporting transactions that may bring public disapproval; for example, those allegedly involving human rights abuses. It is important that EDC meets the highest standards when it puts a Canadian face on exports.

96. EDC’s environmental review policy is part of a larger suite of business ethics practices that EDC states are “integral to its processes when analyzing finance and insurance transactions.” EDC has taken steps to enhance its ability to obtain and analyze relevant social information. It has a memorandum of understanding with Foreign Affairs Canada to share information on the human rights policies and records of various countries with EDC’s Political Risk Assessment Department.

97. We found that EDC’s Environmental Advisory Services team reviewed social assessment information for certain transactions; EDC’s Political Risk Assessment Department dealt with human rights issues in other cases. However, the broad nature of social issues can make it difficult to determine where the responsibility lies to review these issues. EDC has no over-arching policy to co-ordinate the activities undertaken in its various departments to address broader social issues in a coherent fashion and to ensure that no significant risks are overlooked.

98. **Recommendation.** EDC should adopt a policy to ensure that risk analysis of the social impacts of transactions is co-ordinated among its various departments.

EDC’s response. EDC believes that it is important to consider the environmental and related social effects of the projects it is asked to support. The Environmental Review Directive defines “environmental effect” as “any change in the environment, including any project-related social impact...”. More specifically, the Directive reflects the precept of the OECD’s Common Approaches agreement that “any instance of involuntary resettlement or any other adverse change that the project imposes on indigenous or vulnerable groups or on cultural heritage” comprises a potential “social impact” which might be caused by a project.

EDC considers human rights as a regular part of its due diligence, through mechanisms which are additional to those processes dedicated to environmental and social impact review. For example, exchanges between EDC and the Department of Foreign Affairs on human rights issues internationally are separate from the Directive and the mechanics are managed by country experts in EDC’s Political Risk Assessment Department (PRAD). PRAD’s assessments are documented in the Memorandum of Authorization required to proceed with transactions and are considered part of EDC’s overall risk assessment process. As recommended by the

Office of the Auditor General, EDC will review its current approach to ensure maximum efficiency in these mutually supportive processes.

Conclusion

99. We found that EDC's Environmental Review Directive and other environmental review processes contain most (34 of 37) elements of a suitably designed environmental review policy. EDC has designed its environmental review policies to be in line with the *OECD Recommendation on Common Approaches on Environment and Officially Supported Export Credits*.

100. We found that EDC has made major improvements to the manner in which it implemented its environmental review processes, including the Directive. Overall, we concluded that the Directive and other review processes were operating as designed.

101. EDC has built considerable discretion into its Directive and other environmental review processes. While we found EDC was careful in exercising its professional judgment, we noted areas for improvement in documenting how it exercises this discretion: analysis of environmental impact assessment reports and public consultation.

102. Increased expectations for greater accountability in both the private and public sectors impose on EDC a greater responsibility to demonstrate that it exercises its discretion wisely. In our view, the counterbalance to the broad discretion in EDC's environmental review policies is greater transparency. Although EDC filled some of the transparency gaps we noted previously, our Report recommends additional steps that EDC needs to take to enhance transparency and to assure Parliament and Canadians that EDC's environmental review processes uphold high standards of environmental protection and sustainable development.

103. In our last audit, we found that EDC was a leader among the G-8 export credit agencies in terms of environmental policies despite criticisms about lack of consultation or public disclosure. Today many other export credit agencies have caught up, particularly with respect to transparency aspects. In our view, EDC should decide whether it wishes to show leadership among export credit agencies by enhancing its Directive and other review processes.

EDC's overall response. *EDC is pleased to receive the findings of the Office of the Auditor General's (OAG) Report, which acknowledge EDC's significant efforts and achievements in designing and implementing its Environmental Review Directive and associated processes. The key audit findings confirm both the suitability of the design of the Directive and associated processes and that these have been implemented as designed. The improvements noted in the findings have been achieved in a short period of only two years since the previous OAG audit in this area, attesting to EDC's commitment to environmental review, and its dedication to continually improve its practices.*

EDC agrees with the OAG that EDC and other export credit agencies operate in a climate of escalating expectations regarding transparency, public trust, and accountability. It is equally true, however, that these agencies operate in a world of escalating global competition in which exporters and investors are demanding effective global trade tools and increasingly need a sophisticated suite of export development programs and risk management products. One of EDC's fundamental responsibilities in fulfilling its mandate is to strike a balance between the needs of Canada's exporters and the expectations that exist around environmental review.

With respect to international leadership, EDC believes that it continues to play a leading role among export credit agencies in many areas of environmental review and related disclosure practices. These are areas of rapid evolution, and in many areas international norms are still emerging. No single agency has established a leadership position on all of the many elements of environmental review. Moreover over the past few years, agencies have demonstrated their commitment to on-going co-operation and co-ordination at the OECD level to develop a consistent and appropriate global playing field for their respective exporters with respect to environmental review and disclosure. As the yardsticks continue to move, EDC is of the view that leadership is most appropriate in the context of the OECD discussions and that the Corporation should continue to play a leadership role in this forum.

The OAG's Report emphasizes the importance of accountability and transparency. EDC's Disclosure Policy has been effective in encouraging project sponsors to release environmental information on projects. Since the last OAG Report in 2001, EDC has created the position of Chief Environmental Advisor and a stand-alone Environmental Advisory Services Group with an extensive role in conducting environmental reviews and risk assessments and in identifying appropriate mitigation measures related to transactions for which EDC's support has been sought. The Chief Environmental Advisor also has a broader role in engaging with stakeholders and reports quarterly to the Audit Committee of the Board of Directors on various matters including specific transactions reviewed. Further, the Chief Environmental Advisor reports publicly through an annual report, which provides additional information on environmental review at EDC. Together with the reports by EDC's Compliance Officer to the Board of Directors and to the public on EDC's compliance with its environmental and disclosure policies, EDC has created regular channels for promoting accountability and transparency in these areas.

Given EDC's mandate to support and develop export trade, and the heightened public expectations around environmental review, EDC has regularly met with a range of stakeholders on environmental review matters. These stakeholders include exporters, business associations, and a broad range of non-governmental organizations interested in environmental and corporate social responsibility issues. These exchanges, along with the proactive dissemination of information on environmental and other corporate social responsibility practices, as well as active participation in conferences and forums focussing on these issues, round out EDC's approach to transparency of, and accountability on, its conduct.

About the Audit

Scope and approach

We used a two-phase approach similar to our 2001 audit of EDC's environmental review processes.

Design suitability. First, we looked at whether Export Development Canada's Environmental Review Directive and other review processes were suitably designed. We based our review on the criteria for a suitably designed environmental review process that we used for our 2001 audit. These criteria were developed using the following steps:

- We examined the findings from a study on the environmental and social requirements of international financial institutions carried out under the guidance of the World Bank Group's International Finance Corporation. Export credit agencies were among the 42 institutions that participated in this study, which defined minimum requirements of good practice that international financial institutions should adopt to ensure that the projects they support are environmentally and socially responsible. These minimum requirements correspond to the main elements of our audit criteria.
- We developed sub-elements based on our Office's 1998 audit of environmental assessment (May 1998 Report of the Commissioner of the Environment and Sustainable Development, Chapter 6, Environmental Assessment—A Critical Tool for Sustainable Development). The criteria we used in our 1998 audit defined good environmental assessment practice.
- We categorized our sub-elements into standard or emerging elements. Standard elements are used by a majority of institutions; emerging elements are used only by a minority of institutions. To validate our categorization, we examined the environmental review policies of several organizations, including the export credit agencies of Canada's main trade competitors. We focussed on documented policies but did not examine how they were put into practice.

We updated the information used in our previous benchmarking exercise by examining the most recent environmental review policies and procedures of 18 institutions, including export credit agencies that are EDC's competitors, multilateral and bilateral organizations engaged in international project support, and one Canadian and one foreign commercial bank with international lending practices. We used publicly available information for our work to compare policies. We are not in a position to verify the accuracy of this information nor to audit the application by other institutions of their environmental review policies.

To determine whether EDC's Environmental Review Directive and other environmental practices were suitably designed, we applied the standard elements as our audit criteria. We applied the emerging elements to indicate the steps EDC could take to strengthen its Directive and other environmental review processes.

Implementation. In the second phase, we assessed the extent to which the Directive and other procedures were implemented as designed. We developed a checklist of the key features of the Environmental Review Directive and other review processes used by EDC and applied it to a series of transactions reviewed by EDC during the period from 21 December 2001 to 31 December 2003 as follows:

- a sample of 11 (of 17) transactions classified as Category A, B, and C projects under the Environmental Review Directive;
- a sample of 8 (of 33) transactions classified as Category A and B projects that EDC reviewed under other environmental procedures;
- a sample of 21 (of over 3000) transactions not related to a project, with a focus on higher risk industrial sectors; and
- a sample of 10 (of 29) transactions subject to monitoring obligations.

We interviewed EDC staff and corporate officials, including financial services managers involved in the selected transactions, the Environmental Advisory Services team, and members of Internal Audit and Evaluation. We also interviewed clients of Export Development Canada as well as representatives from other export credit agencies and civil society organizations.

Audit team

Assistant Auditor General: Richard Flageole

Commissioner of the Environment and Sustainable Development: Johanne G  linas

Principal: Stuart Barr

Director: Darlene Pearson

Pierre Fr  chette

For more information, please contact Communications at (613) 995-3708 or 1-888-761-5953 (toll-free).

Appendix A Environmental Review Directive

Preamble

1. For the purposes of section 10.1 of the *Export Development Act*, this Environmental Review Directive (the “directive”) sets out the process by which Export Development Canada (“EDC”) will, before entering into a transaction that is related to a project, determine whether the project is likely to have adverse environmental effects despite the implementation of mitigation measures and, if so, whether EDC is justified in entering into the transaction.
2. The directive requires EDC to categorize relevant projects on the basis of their potential adverse environmental effects; categorization determines the nature and extent of environmental information that will be required by EDC in conducting its environmental review of the project, as well as the extent of that review.
3. Where the directive requires that EDC conduct an environmental review of a project, EDC will use international standards as benchmarks. The directive establishes grounds upon which EDC is justified in entering into a transaction related to a project where that project, despite the implementation of mitigation measures, is likely to have adverse environmental effects.
4. The directive also prescribes those projects in respect of which EDC is not required to conduct an environmental review, and sets out exceptions to the obligation to make the determination referred to above. Finally, the directive provides, in Annex 1, definitions of various terms used herein.

Scope

5. This directive applies in all instances in which EDC is considering exercising its powers under section 10 or 23 of the *Export Development Act* by entering into a transaction that has, as applicable, a repayment term or coverage period of two years or more and a value of more than SDR 10 million and that is related to a project. A transaction is related to a project if, in EDC’s opinion, it is: (i) in respect of goods or services purchased or to be purchased (or with respect to which rights of use are otherwise acquired), by a project sponsor, project company or an entity with prime responsibility for project design, development and construction, for use in a particular identified project; (ii) in respect of an equity transaction or an equity investment made in a particular identified project by or on behalf of a project sponsor; or (iii) entered into by EDC for the purpose of promoting procurement of Canadian goods or services by a project sponsor, project company or other entity with prime responsibility for project design, development and construction, for use in a particular identified project.

Categorization

6. In respect of each transaction to which this directive applies, EDC will categorize the related project on the basis of the extent of the project’s potential adverse environmental effects, which categorization will determine the nature and extent of environmental information that will be required by EDC in conducting its environmental review of the project, as well as the extent of that review. EDC’s categorization of a project into one of the following three categories will reflect EDC’s evaluation of the most appropriate category for the project in question. Where EDC determines that its categorization of any project is inappropriate, EDC will re-categorize the project.

Category A

7. EDC will categorize a project in Category A if EDC considers that the project is likely to have significant adverse environmental effects that are sensitive, diverse, or unprecedented. These effects may affect an area broader than the sites or facilities subject to the physical works, and may be irreversible. For illustrative purposes only, Annex 2 provides a list of sensitive sectors and projects that will generally be considered by EDC, for the purposes of categorization, to be Category A projects.
8. The environmental assessment for a Category A project will normally be in the form of an environmental impact assessment (a report with respect to which is illustrated in Annex 3), but may be comprised of elements of other EA instruments including any of those referred to in Annex 4.
9. EDC expects that for each Category A project public consultations with affected parties, if any, will be held in the host country, and that the results of these consultations will have been taken into account in the environmental

assessment of the project. EDC's expectations regarding the nature, scope and extent of public consultation will take into account the political, legal, and cultural context of the host country.

Category B

10. EDC will categorize a project in Category B if EDC considers that the project's potential environmental effects are less adverse than the potential environmental effects of Category A projects. Environmental effects associated with Category B projects are usually site-specific; few if any are irreversible; and in most cases mitigation measures can be designed more readily than for Category A projects.
11. The scope of environmental assessment for a Category B project may vary from project to project, and is more narrow than that of an EA for a Category A project.

Category C

12. EDC will categorize a project in Category C if EDC considers that the project is likely to have minimal or no adverse environmental effects. Generally, no environmental assessment is required for Category C projects.

Environmental Review Information Requirements

13. The information EDC will require in connection with its environmental review of a project will vary depending upon the category into which the project has been classified by EDC.
14. In all cases, the submission to EDC of existing documentation is encouraged to improve the efficiency of the review process and minimize duplication of effort. Where an environmental analysis of a project has been conducted by a recognized international financial institution whose environmental review procedures are acceptable to EDC, EDC may consider such institution's environmental analysis of the project in conducting its own review.
15. Where a project is located in either of Canada or the United States of America and EDC receives confirmation that the project has been designed in compliance with host country environmental requirements, EDC may determine that it requires no additional environmental information in respect of the project beyond that required for categorization.
16. Where EDC determines that it is unable to obtain sufficient environmental assessment information to conduct its environmental review of a project, EDC will decline to enter into a transaction related to such project.

Category A projects

17. For Category A projects, EDC will require a copy of the EIA report (or comparable EA instrument reports) or elements thereof in order to assist EDC in identifying and assessing potential adverse environmental effects associated with the project.
18. If the environmental assessment for a Category A project has been completed by an employee(s) of the project sponsor or project company, or an employee(s) of any affiliate thereof, EDC will require, prior to the time it enters into a transaction related to the project, that independent expertise acceptable to EDC be engaged to review such environmental assessment for potentially significant problems in the analysis.

Category B projects

19. Environmental information provided to EDC for the purposes of an environmental review of a Category B project may be in the form of EA instrument reports or elements thereof, in order to assist EDC in identifying and assessing potential adverse environmental effects associated with the project. In addition, EDC may accept various approaches to meeting its informational requirements for Category B projects: for example, environmentally-sound design criteria, or pollution standards for small-scale industrial plants or rural works; environmentally-sound siting criteria, construction standards, or inspection procedures for housing projects; or environmentally-sound operating procedures for road rehabilitation projects.

Category C projects

20. No environmental assessment information is required by EDC in respect of a Category C project, except as may be required by EDC to categorize the project.

Evaluation and Decision

21. In conducting its environmental review, EDC will use, as benchmarks, the international standards which are in EDC's opinion the most appropriate to the particular project, and require any adverse gaps EDC identifies between the standards to which the project has been designed and the international standards selected by EDC to be explained to EDC's satisfaction.
22. In addition, the environmental assessment information provided will demonstrate to EDC's satisfaction that the project in respect of which EDC is conducting a review has been designed to comply with host country environmental requirements, such as any applicable provisions for local consultation, licenses, permits and other regulatory approvals.
23. On the basis of its environmental review, EDC will come to a conclusion as to whether or not a project is likely to have adverse environmental effects despite the implementation of mitigation measures. In the event that EDC has completed its environmental review and is of the view that a project is likely to have adverse environmental effects despite the implementation of mitigation measures, EDC will determine whether, despite these effects, EDC is justified in entering into a transaction in respect of such project.
24. Grounds which in EDC's view justify providing support to a project that has adverse environmental effects despite mitigation measures include:
 - the adverse environmental effects, taking into account mitigation measures, associated with the project are not in EDC's view significant;
 - EDC's satisfaction that the project is designed to meet or exceed internationally recognized good practices, guidelines or standards;
 - the existence of what are in EDC's view compelling socio-economic considerations as presented by the host country;
 - the project represents an opportunity to improve environmental conditions in the host country above base-line conditions; or
 - the project provides the opportunity to transfer environmentally sound technologies, services and knowledge to, or for the benefit of, the host country.
25. Where EDC determines that it is justified in entering into a transaction related to a project that is likely to have adverse environmental effects despite the implementation of mitigation measures, EDC may (but need not) enter into the transaction.
26. Where EDC determines that it is not justified in entering into a transaction related to a project that is likely to have adverse environmental effects despite the implementation of mitigation measures, EDC will decline to enter into the transaction.

Covenants and Monitoring

27. Compliance by a project with host country laws and regulations will normally be confirmed through warranties and representations.
28. Where EDC's environmental review identifies a need to monitor a project, EDC will seek to obtain such rights, assurances or covenants as EDC deems necessary to provide to it the ability to conduct such monitoring during the term of EDC's support to the project. Where EDC is unable to secure such rights, assurances or covenants as it deems necessary in the circumstances, EDC may decline to enter into the transaction.

Exceptions

29. Notwithstanding anything else herein, EDC shall not be required to make a determination for the purposes of section 10.1 of the *Export Development Act* in respect of:

- a) any transaction related to a project EDC was, as of December 21, 2001, already reviewing under the Environmental Review Framework;
- b) any transaction related to a project in respect of which, as of December 21, 2001, an approval for any purpose has been given by any level of authority within EDC or an endorsement has been made by the Risk Management Office of EDC or the management Risk Management Committee;
- c) any transaction related to a project that is in support of a review or study in connection therewith, such as an environmental or feasibility study;
- d) any transaction related to a Category C project; and
- e) any transaction related to a Category A or B project which is located in Canada or the United States of America, where EDC receives confirmation that the project has been designed in compliance with applicable host country environmental requirements.

30. Transactions related to projects described in 29 a), b) and c) above are entirely exempt from the application of this directive. EDC will categorize projects referred to under 29 d) and e) above in accordance with this directive, but EDC is not required to make a determination in respect of same.

Effective Date

31. This amended directive, which is not retroactive, shall come into effect on May 1, 2002 and shall replace the directive which came into effect on December 21, 2001.

Annex 1—Definitions

Definitions

The following terms shall have the meanings ascribed thereto below when used in this directive:

“adverse environmental effect” means any harmful environmental effect;

“affected parties” means those parties living at or near the site of the project, indigenous groups with an interest in project land, project sponsors and local non-governmental or public sector organizations participating in the local public consultation process;

“considering”, in relation to a transaction and for the purposes only of the Scope of this directive, means that EDC is prepared, but for the application of the directive, to enter into the transaction;

“coverage period” means the time period starting from the day that insurance coverage provided under a policy issued by EDC in a political risk insurance transaction commences to apply through to and including the date upon which such coverage would normally be expected to terminate in accordance with the terms of such policy;

“enter”, in relation to a transaction related to a project, means the point of time at which EDC first becomes unconditionally legally obligated to provide funds to its transaction counterparty, or at which EDC’s political risk insurance coverage commences to apply;

“environment” means land, water, air, living organisms and interacting natural systems;

“environmental assessment” or **“EA”** means the process of assessing the environmental effects and project-related social impacts of a project in order to evaluate their significance, and may include identifying measures to prevent, minimize, mitigate or compensate for adverse environmental effects. Environmental assessment is the responsibility of the project sponsor;

“environmental assessment instruments” or **“EA instruments”** are tools used to assess the environmental effects and project-related social impacts of a project in order to evaluate their significance, which may also identify measures to

prevent, minimize, mitigate or compensate for adverse environmental effects; EA instruments include EIAs and other instruments described in Appendix 4;

“environmental effect” means any change to the environment, including any project-related social impact, as a result of the normal construction or operation of the project, or in the event of a reasonably foreseeable accident or malfunction in relation to the project;

“environmental impact assessment” or **“EIA”** means an EA instrument to identify and assess the potential environmental effects of a project, evaluate alternatives, and design mitigation, management and monitoring measures;

“environmental impact assessment report” or **“EIA report”** means the document or documents which describe the processes, findings and conclusions of the EIA;

“environmental review” means the review by or for EDC of the environmental assessment of a project;

“Environmental Review Framework” means the framework, employed by EDC in conducting environmental reviews of projects related to transactions EDC was considering, which came into effect on April 12, 1999;

“equity transaction” means the acquisition by EDC, other than by way of the taking or realization of security or recovery, of an interest in an entity in the exercise of its powers under subsection 10(1.1) of the *Export Development Act*;

“Export Development Act” means the Export Development Act (R.S.C. 1985, c. E-20), as amended from time to time;

“financing transaction” means a loan, any facility whereby EDC purchases receivables whether or not such receivables are evidenced by debt instruments, lease or financing guarantee entered into by EDC pursuant to EDC's financing program;

“greenfield” means, in relation to a project, developed on a previously undeveloped site or location;

“host country” means the nation in which a project is located;

“international standards” means the internationally recognized good practices, standards and guidelines with respect to project design and performance that EDC will rely upon as benchmarks in undertaking its environmental review of a project; an illustrative list of such good practices, standards and guidelines is provided in Annex 5;

“major extension” means, in relation to a project, additions or modifications intended to result in a substantial change in output or functionality;

“mitigation measures” means methods to reduce, eliminate or compensate for adverse environmental effects;

“political risk insurance transaction” means insurance coverage provided by EDC under its political risk insurance program to protect against political risks such as foreign exchange transfer difficulties, expropriation by a host government, or war, revolution, and insurrection;

“project” means a physical development that is greenfield, or undergoing major extension or transformation-conversion and is industrial, commercial or infrastructure-related in nature;

“project-related social impact” means any instance of involuntary resettlement or any other adverse change that the project imposes on indigenous or vulnerable groups or on cultural heritage;

“project company” means an entity owned in whole or in part by a project sponsor and established for the purpose of the design, development, construction or operation of a particular identified project;

“project sponsor” means an entity owning, either directly or through an ownership interest in a project company, the assets of a project;

“repayment term” shall have the meaning given that term in section 8 of the Arrangement on Guidelines for Officially Supported Export Credits;

“SDR” means Special Drawing Rights, an artificial currency unit defined as a basket of national currencies established by the International Monetary Fund;

“transformation/conversion” means, in relation to a project, reuse on a previously developed site or a modernization intended to result in a substantial change in output or functionality; and

“transaction” means EDC’s support of a project in the form of financing, political risk insurance or equity, or any combination thereof, in cases which that support has, as applicable, a repayment term or coverage period of two years or more and a value of more than SDR 10 million.

Annex 2—Illustrative List of Category A Projects

I. Projects as described below:

1. Crude oil refineries (excluding undertakings manufacturing only lubricants from crude oil) and installations for the gasification and liquefaction of 500 tonnes or more of coal or bituminous shale per day.
2. Thermal power stations and other combustion installations with a heat output of 300 megawatts or more and nuclear power stations and other nuclear reactors (except research installations for the production and conversion of fissionable and fertile materials, whose maximum power does not exceed 1 kilowatt continuous thermal load).
3. Installations solely designed for the production or enrichment of nuclear fuels, the reprocessing of irradiated nuclear fuels, or for the storage, disposal and processing of radioactive waste.
4. Major installations for the initial smelting of cast iron and steel and for the production of nonferrous metals.
5. Installations for the extraction of asbestos and for the processing and transformation of asbestos and products containing asbestos: for asbestos-cement products, with an annual production of more than 20,000 tonnes finished product; for friction material, with an annual production of more than 50 tonnes finished product; and for other asbestos utilisation of more than 200 tonnes per year.
6. Integrated chemical installations including the manufacture and transportation of pesticides and hazardous/toxic materials.
7. Construction of motorways, express roads and lines for long-distance railway traffic and of airports with a basic runway length of 2,100 metres or more.
8. Large-diameter oil and gas pipelines.
9. Sea ports and also inland waterways and ports for inland-waterway traffic which permit the passage of vessels of over 1,350 tonnes.
10. Waste-disposal installations for the incineration, chemical treatment or landfill of toxic and dangerous wastes.
11. Large dams and reservoirs.
12. Groundwater abstraction activities in cases where the annual volume of water to be abstracted amounts to 10 million cubic metres or more.
13. Pulp and paper manufacturing of 200 air-dried metric tonnes or more per day.
14. Major mining, on-site extraction and processing of metal ores or coal.
15. Hydrocarbon production.
16. Major storage facilities for petroleum, petrochemical and chemical products.
17. Large-scale logging.
18. Large-scale waste-water treatment.
19. Domestic solid waste-processing facilities.
20. Large-scale tourism development.
21. Large-scale power transmission.
22. Large-scale reclamation.
23. Large-scale agriculture/silviculture involving the intensification or development of previously undisturbed land.

24. Tanneries.

II. Sensitive Areas

A project may also be classified as Category A if it is planned to be carried out in a sensitive location, even if it does not otherwise appear in the above list. These sensitive areas include National Parks and other conservation areas of national or regional importance, such as wetlands and areas of archaeological significance, areas prone to erosion and/or desertification, and areas of importance to ethnic groups. The preceding list is clearly non-exhaustive and the types of projects it contains are examples only.

Annex 3—Illustrative Environmental Impact Assessment Report

An EIA's scope and level of detail should be commensurate with the project's potential environmental effects. The EIA report will normally include the following items*:

- Executive Summary: Concisely discusses significant findings and recommended actions.
- Policy, legal and administrative directive: Discusses the policy, legal, and administrative directive within which the EIA is carried out.
- Project description: Describes the proposed project and its geographic, ecological, social, and temporal context, including any offsite investments that may be required (e.g., dedicated pipelines, access roads, power plants, water supply, housing, and raw material and product storage facilities). Indicates the need for any resettlement or social development plan. Normally includes a map showing the project site and the project's area of influence.
- Baseline data: Assesses the dimensions of the study area and describes relevant physical, biological, and socio-economic conditions, including any changes anticipated before the project commences. Also takes into account current and proposed development activities within the project area but not directly connected to the project. Data should be relevant to decisions about project location, design, operation, or mitigation measures. The section indicates accuracy, reliability and sources of the data.
- Environmental effects: Predicts and assesses the project's likely positive and negative effects. Identifies mitigation measures and any residual negative effects that cannot be mitigated. Explores opportunities for environmental enhancement. Identifies and estimates the extent and quality of available data, key data gaps, and uncertainties associated with predictions, and specifies topics that do not require further attention.
- Analysis of alternatives: Compares feasible alternatives to the proposed project site, technology, design and operation including the "without project" situation. For each of the alternatives, quantifies the environmental effects to the extent possible, and attaches economic values where feasible. States the basis for selecting the particular project design proposed and justifies recommended emission levels and approaches to pollution prevention and abatement.
- Environmental Management Plan: Describes mitigation, monitoring and institutional measures to be taken during construction and operation to eliminate adverse effects, offset them, or reduce them to acceptable levels.
- Consultation: Record of consultation meetings, including consultations for obtaining the informed views of the affected people, local non-governmental organizations and regulatory agencies.
- Appendices.

**Note that the lack of one or more of these elements in an EIA report does not necessarily mean that the report or the related EIA is incomplete.*

Annex 4—Other Environmental Assessment Instruments

"environmental audit" means an instrument to determine the nature and extent of all environmental areas of concern at an existing facility. The audit identifies and justifies appropriate measures to mitigate the areas of concern, estimates the cost of the measures, and recommends a schedule for implementing them. For certain projects, the EA report may consist of an environmental audit alone; in other cases, the audit is part of the EA documentation;

“environmental management plan” (EMP) means an instrument that details (a) the measures to be taken during the implementation and operation of a project to eliminate or offset adverse environmental effects, or to reduce them to acceptable levels; and (b) the actions needed to implement these measures. The EMP is an integral part of Category A EAs (irrespective of other instruments used). EAs for Category B projects may also result in an EMP;

“hazard assessment” means an instrument for identifying, analyzing, and controlling hazards associated with the presence of dangerous materials and conditions at a project site. Hazard assessments should be undertaken for projects involving certain inflammable, explosive, reactive, and toxic materials when they are present at a site in quantities above a specified threshold level. For certain projects, the EA report may consist of the hazard assessment alone; in other cases, the hazard assessment is part of the EA documentation;

“environmental risk assessment” means an instrument for estimating the probability of harm occurring from the presence of dangerous conditions or materials at a project site. Environmental risk represents the likelihood and significance of a potential hazard being realized; therefore, a hazard assessment often precedes a risk assessment, or the two are conducted as one exercise. Environmental risk assessment is a flexible method of analysis, a systematic approach to organizing and analyzing scientific information about potentially hazardous activities or about substances that might pose risks under specified conditions. Environmental risk assessments should be undertaken for projects involving handling, storage, or disposal of hazardous materials and waste, the construction of dams, or major construction works in locations vulnerable to seismic activity or other potentially damaging natural events. For certain projects, the EA report may consist of the risk assessment alone; in other cases, the environmental risk assessment is part of the EA documentation.

Annex 5 – Illustrative List of Internationally Recognized Good Practices, Standards and Guidelines

- World Bank’s Pollution Prevention and Abatement Handbook.
- The International Finance Corporation’s Guidelines and Safeguard Policies.
- The environmental requirements, standards, policies or guidelines of regional development banks (such as the African Development Bank, Asian Development Bank, European Bank for Reconstruction and Development and the Inter-American Development Bank).
- Canadian Council of Ministers of the Environment (CCME): Canadian Environmental Quality Guidelines.
- World Health Organization (WHO): Air Quality and Drinking Water Quality Guidelines.
- Good practices guidelines published by United Nations Environment Programme.
- Good practices guidelines published by internationally recognized industry associations such as Responsible Care, International Council on Metals and the Environment or International Atomic Energy Agency.
- International Organization for Standardization: ISO 14000 standards.

